

This letter discusses claims for credit under the Tobacco Products Tax Act of 1995. See 35 ILCS 143/10-1 et seq. (This is a GIL).

October 30, 2002

Dear Xxxxx:

This letter is in response to your letter dated July 15, 2002. The nature of your letter and the information you have provided require that we respond with a General Information Letter, which is designed to provide general information, is not a statement of Department policy and is not binding on the Department. See 2 Ill. Adm. Code 1200.120 subsections (b) and (c), which can be found at <http://www.revenue.state.il.us/Laws/regs/part1200/>.

In your letter, you have stated and made inquiry as follows:

Please accept this letter as a request for a private ruling by the Illinois Department of Revenue (the 'Department') regarding the availability of credits for taxes paid on tobacco products returned to the manufacturer and the appropriate responsibility for payment of tax under 35 Ill. Comp. Stat. 143/10-10 with respect to replacement products.

FACTS

AAA is engaged in the promotion and sale of smokeless tobacco products in the State of Illinois and elsewhere throughout the United States. AAA holds a valid Illinois tobacco products distributor license. Most of AAA's customers are licensed wholesale distributors who resell the products to retailers and remit the tax on tobacco products. AAA purchases the tobacco products exclusively from BBB. Both AAA and BBB are wholly owned subsidiaries of CCC.

Current Returned Goods Procedures

AAA employs sales representatives ('Sales Reps'), who act as representatives for the Company. These Sales Reps, furnished with company cars and a supply of stock ('car stock'), provide a service on behalf of its distributors by traveling to retail customers to sample and otherwise promote the sale of the Company's tobacco products and to regularly replace outdated or damaged products ('returned products') with car stock. Returned products are accumulated by Sales Reps and periodically exchanged for an equivalent amount of fresh products ('replacement products') through certain of the Company's wholesale distributor customers ('Central Service Jobbers' or 'CSJs'). CSJs ship returned products back to BBB's manufacturing facility where BBB accepts such products on behalf of AAA and issues affidavits of their return to the CSJ and AAA. AAA then issues a refund or credit to the CSJ for the original purchase price of the tobacco products. Currently, CSJs pay the tobacco tax on replacement products and obtain a

credit for tax paid on returned products. AAA pays the tobacco tax on the initial issuance of car stock at the time it is first received by Sales Reps.

Proposed Changes to Returned Goods Procedures

AAA is considering changing the manner in which it processes replacement and returned products (the 'Proposed Change'). Sales Reps will continue to replace outdated or damaged products with their available car stock. Under the Proposed Change, however, Sales Reps (not CSJs) will ship returned products directly to BBB's manufacturing facility. BBB will accept such products on behalf of AAA and issue affidavits of their return solely to AAA. Furthermore, under the Proposed Change, Sales Reps will order replacement product (in order to replenish their car stock) directly from AAA rather than through a CSJ. AAA will accordingly ship replacement products directly to the Sales Rep.

Note, AAA will ship car stock to locations where AAA rents warehouse space for Sales Rep pickup. These locations for the most part coincide with our distributors' locations.

Under the Proposed Change, AAA will separately account for each transaction (i.e., the sale of replacement product and the credit sale of returned product) on its books and records. Note that although a Sales Rep exchanges tobacco products on a can-for-can basis, a Sales Rep's order of replacement stock will generally not equal the number of cans returned at any one point in time. This difference, which is due primarily to timing, may result in a net tax liability or credit in any particular tax reporting period. For example, a Sales Rep may order two cases of replacement product on December 31st but not ship two cases of returned products back to the manufacturer until the following month when he accumulates a substantial quantity of products to return. Consequently, should these be the only transactions that occur within these respective monthly tax reporting periods, a tax would be due in December and an equal amount of tax would be credited in January.

Note that under the Proposed Change, CSJs will no longer be paying tax on replacement products ordered by a Sales Rep or filing for tax credits on products returned by a Sales Rep since the new process will not involve the CSJ.

Request for Ruling

Based on the facts above, we respectfully request a ruling regarding the following:

1. Whether, under AAA's Proposed Change, AAA is liable for the tobacco products tax when replacement product is received by Sales Reps?

It appears that AAA would be liable for tobacco products tax when AAA ships car stock to Sales Reps, which Sales Reps then use to replace outdated or damaged product at retailers' locations. Under Illinois statute a tobacco products tax is imposed on 'any person engaged in business as a distributor of tobacco products...[on] the wholesale price of tobacco products sold or otherwise disposed of to retailers or consumers located in this State.' 35 Ill. Comp. Stat. 143/10-10. 'Sale' means any transfer, exchange, or barter in any manner or by any means whatsoever for a consideration and includes all sales made by persons. 35 Ill. Comp. Stat. 143/10-5. Consequently, when a Sales Rep

exchanges outdated product with replacement product, AAA, a properly licensed distributor, would be treated as 'selling' such tobacco products and would be liable for the tobacco products tax.

2. Whether, under AAA's Proposed Change, AAA is entitled to receive credits for the taxes paid on products returned by its Sales Reps?

Based on Form TP-I, Ln.6, Form TP-I Instructions and discussions with the Department, it is our understanding that the Department generally allows a credit for taxes paid on tobacco products that are unfit for use or returned to the manufacturer. AAA (through its Sales Reps) will return outdated and damaged tobacco products to BBB, their manufacturer. Since AAA will be required to pay tobacco products tax on replacement products, it should therefore be entitled to a credit for damaged and outdated tax-paid product received from retailers and returned to the manufacturer through its Sales Reps in exchange for such replacement product. Once again, it should be noted that under the Proposed Change, CSJs will no longer be paying tax on replacement products ordered by Sales Reps or claiming tax credits on products returned by Sales Reps.

As indicated previously, CSJs currently pay tax on Sales Rep replacement product and receive a tax credit for products returned to AAA. The only difference under the Proposed Change, is that product will be returned to, and replacement product will be ordered directly from, AAA, not the CSJ. Since the retail transaction has not changed, it would be logical under the statutes that AAA should be liable for the tobacco products tax and entitled to the same tax credits currently taken by the CSJ when it returns product to BBB.

Since the Company anticipates the rollout of the Proposed Change within the next few months, we would greatly appreciate your expedience in this matter. If you need any further information or have any questions, please do not hesitate to contact me.

Under the Tobacco Products Tax Act of 1995 (35 ILCS 143/10-1 et seq.) the Tobacco Products Tax is imposed upon the last distributor who sells tobacco products to a retailer or consumer located in Illinois at the rate of 18% of the wholesale price of tobacco products sold or otherwise disposed of in this State. Not all sales of tobacco products by distributors or wholesalers are subject to tax. For example, sales by a distributor to another distributor as sales for resale are exempt from the tax imposed by this Act.

If it appears, after claim therefore filed with the Department, that an amount of tax or penalty has been paid that was not due under the Act, whether as a result of a mistake of fact or an error of law, then the Department shall issue a credit memorandum or refund to the person who made the erroneous payment.

If a distributor, such as AAA, pays the tobacco tax when it sells tobacco products to a retailer, then agrees to exchange the outdated tax-paid tobacco products for replacement tobacco products, AAA may file a claim for credit for the tax paid on the outdated tobacco products. Please note that the distributor may not file a claim for credit for any tax that it did not pay. Also, the distributor that sells the replacement tobacco products to the retailer must pay the tobacco tax on the replacement tobacco products that it sells or otherwise disposes of.

I hope this information is helpful. The Department of Revenue maintains a Web site, which can be accessed at www.revenue.state.il.us. If you have further questions related to the Illinois sales tax laws, please contact the Department's Taxpayer Information Division at (217) 782-3336.

If you are not under audit and you wish to obtain a binding Private Letter Ruling regarding your factual situation, please submit all of the information set out in items 1 through 8 of Section 1200.110(b).

Very truly yours,

Martha P. Mote
Associate Counsel

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